

## **FISCAL NOTE**

### **HB 2215 - SB 2164**

March 28, 2007

**SUMMARY OF BILL:** Enacts the “Smoke Free Tennessee Act (SFTA) of 2007” and the “Tennessee Tobacco Retailers Act (TTRA) of 2007.” Prohibits smoking in all public places and places of employment. Revises multiple code provisions concerning the use of tobacco products. Requires the Departments of Health and Labor of Workforce Development to administer and enforce the provisions of the SFTA. Revises multiple code provisions concerning the sale and distribution of tobacco products. Prohibits the use of vending machines to sell and distribute tobacco products. Increases the excise tax on cigarettes from 20 cents to 41 cents per pack. Changes the tax rate on moist snuff from 6.6% of the wholesale price to 35 cents per ounce. Increases the tax on all other tobacco products from 6.6% of the wholesale price to 15.0% of the wholesale price. Reapportions tobacco tax revenues for multiple uses. Requires non-participating manufacturers to pay equity assessments on cigarettes equal to 50 cents per pack. Earmarks equity assessment revenue to statewide health programs as may be provided in the general appropriations act. Authorizes the Department of Agriculture to establish a grant program for tobacco farmers.

### **ESTIMATED FISCAL IMPACT:**

#### **Increase State Revenues –**

**\$11,789,000 / Dept. of Agriculture (for tobacco farmer grants)**

**\$18,844,000 / General Fund**

**\$98,884,000 / Education Fund (for at-risk & ELL programs)**

**\$7,011,000 / Education Fund (K-12)**

**\$4,584,000 / Earmarked to Dept. of Health (for elderly care)**

**\$22,913,000 / Earmarked for statewide health programs**

**\$40,000 / Department of Revenue**

**\$99,000 / Sinking Fund**

**\$95,000 / Dept. of Labor Workforce & Development**

**\$164,259,000 – Total Increase**

**Decrease State Revenues - \$270,000 / Dept. of Agriculture**

**Increase State Expenditures - \$1,777,000 One-Time**

**\$6,522,300 Recurring**

**Increase Local Govt. Revenues – Net Impact - \$4,007,000**

**Increase Local Govt. Expenditures – \$43,000 One-Time\***

**\$38,000 Recurring\***

#### Cigarette Excise Tax Assumptions:

- According to the Department of Revenue (DOR), excise tax collections on cigarettes in FY05-06 were approximately \$115,462,000.
- Current excise tax rate on cigarettes is \$0.20 per pack.
- Estimated number of packs sold in FY05-06 was 577,310,000 ( $\$115,462,000 \div \$0.20 = 577,310,000$  packs).
- Cigarette elasticity is estimated from a variable elasticity schedule depending upon the extent of any excise tax increase.
- Cigarette elasticity rate for proposed increase is estimated to be -0.123.
- Current state sales tax rate on cigarettes is 7.00%.
- Local option sales tax rate on cigarettes is estimated to be 2.25%.
- Current consumer price per pack is estimated to be \$3.19 per pack (excluding sales tax); \$3.49 per pack (including sales tax).
- Increasing the excise tax on cigarettes by \$0.21 per pack would also generate an additional \$0.02 per pack in state and local option sales tax revenue ( $\$0.21 \times 9.25\% = \$0.019$ ).
- The total price increase to the consumer is estimated to be \$0.23 per pack ( $\$0.21$  excise tax increase +  $\$0.02$  incremental sales tax =  $\$0.23$ ).
- Consumer price per pack after the proposed excise tax increase is estimated to be \$3.40 per pack (excluding sales tax); \$3.72 per pack (including sales tax).
- Increasing the excise tax on cigarettes would increase the price per pack to the consumer by an estimated 6.6% ( $\$0.23 \div \$3.49 = 6.6\%$ ).
- Quantity demanded would decrease by an estimated 0.81% ( $6.6\%$  price increase  $\times -0.123$  elasticity rate =  $-0.81\%$ ).
- Quantity demanded in FY07-08 is estimated to be 572,633,789 packs ( $577,310,000 \times \{100.00\% - 0.81\%\} = 572,633,789$  packs).
- Total excise tax collections are estimated to be \$234,780,000 ( $572,633,789$  packs  $\times \$0.41$  excise tax =  $\$234,779,853$ ) in FY07-08.
- Incremental excise tax collections on cigarettes are estimated to be \$119,318,000 ( $\$234,780,000 - \$115,462,000 = \$119,318,000$ ) per year.
- As proposed in this legislation, the apportionment of the increased excise tax revenue will be as follows: \$10,739,000 (or 9.0%) to the Department of Agriculture for grants to tobacco farmers, \$14,318,000 (or 12.0%) to the General Fund, \$90,085,000 (or 75.5%) to the Education Fund earmarked exclusively for at-risk and English language learner (ELL) programs, and \$4,176,000 (or 3.5%) to the Department of Health earmarked for home and community-based care for the elderly.

#### Moist Snuff Tax Assumptions:

- The current tobacco tax on non-cigarette tobacco products is 6.6% of the wholesale cost price.
- Total tobacco tax collections were \$124,872,300 for FY05-06.

- Cigarette tax collections for FY05-06 were approximately \$115,462,000.
- Tobacco tax collections for all non-cigarette tobacco products for FY05-06 is estimated to be \$9,410,300 ( $\$124,872,300 \text{ total} - \$115,462,000 \text{ for cigarettes} = \$9,410,300$ ).
- 50% (or \$4,705,150) of non-cigarette tobacco tax collections for FY05-06 were derived from the sale of moist snuff tobacco.
- Taxable wholesale sales for FY05-06 are estimated to be \$71,290,152 ( $\$4,705,150 \text{ estimated collections} \div 6.6\% \text{ current rate} = \$71,290,152$ ).
- 5.0% annual growth of taxable wholesale sales of moist snuff tobacco under current law.
- Taxable wholesale sales are estimated to be \$78,597,400 for FY07-08 under current law ( $[\$71,290,152 \times 105\%] \times 105\% = \$78,597,393$ ).
- Tobacco tax collections from the sale of moist snuff tobacco is estimated to be \$5,187,400 for FY07-08 under current law ( $\$78,597,400 \times 6.6\% = \$5,187,428$ ).
- The average wholesale price for a standard 1.2 ounce canister of moist snuff tobacco is estimated to be \$3.00 before retailer markup and any applicable sales tax.
- The average number of canisters sold in Tennessee is estimated to be 26,200,000 per year ( $\$78,597,400 \text{ wholesale sales} \div \$3.00 \text{ average wholesale price} = 26,199,133 \text{ canisters}$ ).
- The number of ounces sold in Tennessee is estimated to be 31,440,000 per year ( $26,200,000 \text{ canisters} \times 1.2 \text{ ounces per canister} = 31,440,000 \text{ ounces}$ ).
- The proposed excise tax is estimated to generate approximately \$11,004,000 per year ( $31,440,000 \text{ ounces} \times \$0.35 \text{ tax per ounce} = \$11,004,000$ ).
- The net increase to state tax revenues is estimated to be \$5,817,000 per year ( $\$11,004,000 - \$5,187,400 = \$5,816,600$ ).
- As proposed in this legislation, the apportionment of the increased excise tax revenue will be as follows: \$524,000 (or 9.0%) to the Department of Agriculture for grants to tobacco farmers, \$698,000 (or 12.0%) to the General Fund, \$4,391,000 (or 75.5%) to the Education Fund earmarked exclusively for at-risk and English language learner (ELL) programs, and \$204,000 (or 3.5%) to the Department of Health earmarked for home and community-based care for the elderly.
- Quantity demanded remains relatively constant (any decrease of quantity demanded as a result of the proposed tax is offset by an increase of quantity demanded as a result of population growth).
- According to DOR, this bill would require the affixing of tax stamps onto moist snuff canisters much like the tax stamps affixed to packs of cigarettes.
- According to DOR, the cost to the department for tax stamps would be \$29,500 for every 500,000 tax stamps (5.9 cents each).
- The recurring increase to state expenditures for tax stamps is estimated to be \$1,546,000 per year ( $26,200,000 \text{ canisters} \times \$0.059 \text{ tax stamp cost} = \$1,545,800$ ).

#### Other Tobacco Products Tax Assumptions:

- Actual tobacco tax collections for FY05-06 were \$124,872,300.
- FY05-06 tobacco tax collections from non-cigarette and non-snuff tobacco products are estimated to be \$4,705,000 (\$124,872,300 total - \$115,462,000 for cigarettes - \$4,705,150 for moist snuff = \$4,705,150).
- FY05-06 taxable wholesale sales for these remaining tobacco products is estimated to be \$71,288,000 ( $\$4,705,000 \div 6.6\%$  current rate = \$71,287,879).
- Average base price for non-cigarette and non-snuff tobacco products is estimated to be \$3.50 per package.
- The price increase to the consumer is estimated to be  $([\$3.50 \times 115.0\%] - [\$3.50 \times 106.6\%]) = \$0.29$ .
- The \$0.29 increase represents an 8.3% price increase to consumer ( $\$0.29 \div \$3.50$  base price = 8.29%).
- Elasticity rate of -0.171 for proposed tax increase.
- Quantity demanded is estimated to decrease by approximately 1.4% ( $8.3\%$  price increase  $\times$  -0.171 elasticity = 1.4%).
- Adjusted taxable wholesale sales for FY07-08 are estimated to be \$70,290,000 ( $\$71,288,000 \times [100\% - 1.4\%] = \$70,289,968$ ).
- The increase to tobacco tax revenues resulting from taxable wholesale sales of the remaining tobacco products is estimated to be \$5,839,000 ( $[\$70,290,000 \text{ taxable sales} \times 15.0\% \text{ proposed tax rate}] - \$4,705,000 \text{ FY05-06 collections} = \$5,838,500$ ).
- As proposed in this legislation, the apportionment of this increased tax revenue will be as follows: \$526,000 (or 9.0%) to the Department of Agriculture for grants to tobacco farmers, \$701,000 (or 12.0%) to the General Fund, \$4,408,000 (or 75.5%) to the Education Fund earmarked exclusively for at-risk and ELL programs, and \$204,000 (or 3.5%) to the Department of Health earmarked for home and community-based care for the elderly.

#### Equity Assessment Tax Assumptions:

- According to DOR, approximately 9% of all cigarette sales are from non-participating manufacturers (NPM).
- The number of packs of cigarettes sold by NPM is estimated to be 51,957,900 per year ( $577,310,000 \text{ total packs} \times 9.0\% = 51,957,900 \text{ packs}$ ).
- Total price increase to consumer is estimated to be \$0.78 ( $\$0.21 \text{ excise tax increase} + \$0.50 \text{ equity assessment} + \$0.07 \text{ incremental sales tax revenue} = \$0.78$ ).
- The \$0.78 increase represents a 22.3% price increase to consumer ( $\$0.78 \text{ increase} \div \$3.49 \text{ price} = 22.3\%$ ).
- Elasticity rate of -0.53 for proposed tax increase.
- Quantity demanded is estimated to decrease by approximately 11.8% ( $22.3\% \text{ price increase} \times -0.53 \text{ elasticity} = 11.8\%$ ).

- The number of packs sold in FY07-08 is estimated to be 45,826,900 (51,957,900 X [100% - 11.8%] = 45,826,868 packs).
- The increase to state revenues resulting from the additional 50-cent per pack equity assessment is estimated to be \$22,913,000 per year (45,826,900 packs X \$0.50 = \$22,913,450).
- 100% of equity assessment funds are to be earmarked for statewide health programs.

All Other Assumptions:

- State and local government sales tax is computed on the final retail sales (including any additional excise tax and equity assessments).
- The increase to state revenues resulting from incremental state sales tax is estimated to be \$10,772,000 (\$153,887,000 in incremental excise tax/equity assessment tax X 7.0% state rate = \$10,772,090).
- The apportionment of \$10,772,000 in sales tax revenue would be as follows: \$3,127,000 to the General Fund, \$7,011,000 to the Education Fund, \$495,000 to local governments, \$40,000 to DOR, and \$99,000 to the Sinking Fund.
- The local option sales tax rate is estimated to average 2.25%.
- The increase to local government revenues resulting from incremental local option sales tax is estimated to be approximately \$3,462,000 per year (\$153,887,000 in incremental excise taxes X 2.25% = \$3,462,457).
- The Department of Labor and Workforce Development (DLWD) estimates approximately \$95,000 per year in additional revenue generated from fees and fines.
- Four positions in DLWD (two investigators, one administrative secretary, and one attorney) to implement provisions of this bill.
- The recurring increase to DLWD expenditures is estimated to be \$300,000 per year as a result of the four new positions.
- One-time expenditures for DWLD will increase by approximately \$20,000 for printing of literature, staff training, and software and computer enhancements.
- Four positions in DOR (three Regulatory Officers, one Taxpayer Services Representative) to implement provisions of this bill.
- The recurring increase to DOR expenditures for the four new positions is estimated to be \$202,000 per year.
- One-time expenditures for DOR will increase by approximately \$227,000 for costs related to hiring four new positions and for software and computer enhancements.
- Two positions in the Department of Agriculture (one Agricultural Marketing Specialist 2, one Administrative Secretary)
- The recurring increase to DOA expenditures for the two new positions is estimated to be \$84,300 per year.
- DOA estimates a decrease in departmental revenues of \$270,000 per year from the loss of approximately \$70,000 per year in civil penalty fines and

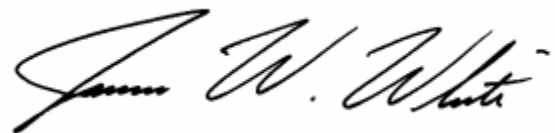
\$200,000 per year from Mental Health & Development Disabilities for funding the Youth Access to Tobacco Act.

- According to the Office of the Comptroller, local governments will incur additional one-time and recurring expenditures estimated to be \$43,000 and \$38,000 respectively as a result of this legislation.
- According to the Office of the Comptroller, local government revenues will increase approximately \$50,000 per year as a result of civil penalty fines.
- Forty-four (44) positions in the Department of Health (DOH) (twenty-four (24) Regulatory Enforcement Agents, three (3) attorneys, eight (8) Administrative Services Assistant positions, eight (8) Environmental Health Specialist 3 positions, and one (1) Human Resource Analyst 3 position) to implement the provisions of this bill.
- The recurring increase to DOH expenditures for the forty-four new positions is estimated to be \$4,390,000 per year.
- One-time expenditures for DOH will increase by \$1,530,000 for costs related to hiring forty-four new positions.

\*Article II, Section 24 of the Tennessee Constitution provides that: *no law of general application shall impose increased expenditure requirements on cities or counties unless the General Assembly shall provide that the state share in the cost.*

### **CERTIFICATION:**

This is to duly certify that the information contained herein is true and correct to the best of my knowledge.

A handwritten signature in black ink, appearing to read "James W. White". The signature is fluid and cursive, with a large initial "J" and a distinct "W".

James W. White, Executive Director